

Message Text

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ACTION TRSE-00

INFO OCT-01 EA-10 NEA-10 ISO-00 L-03 H-01 IO-13 PA-01
SP-02 ICA-11 AID-05 EB-08 NSC-05 SS-15 STR-07
OMB-01 CEA-01 CIAE-00 COME-00 FRB-03 INR-10
NSAE-00 XMB-02 OPIC-03 LAB-04 SIL-01 /117 W
-----070625 100721Z /21
P 100652Z JUL 78
FM AMEMBASSY MANILA
TO SECSTATE WASHDC PRIORITY 8179

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USADB

FOR NAC AGENCIES

PASS TREASURYDEP FOR SHERK

EO 11652:NA
TAGS: EAID, EFIN, ADB
SUBJECT: REVIEW OF ADB LENDING RATE

1. IN FEBRUARY 1978, AT TIME OF FIXING OF ADB LENDING RATE AT 7.65 PERCENT PER ANNUM WITH EFFECT FROM JANUARY 1, 1978, BOARD OF DIRECTORS DECIDED THAT IF IN SECOND CALENDAR QUARTER OF 1978 THE DIFFERENTIAL (0.20 PERCENT) BETWEEN IBRD'S FIRST QUARTER LENDING RATE (7.45 PERCENT) AND BANK'S LENDING RATE SET THEN (7.65 PERCENT) INCREASED OR DECREASED BY FIVE BASIS POINTS (0.05) OR MORE, PRESIDENT WOULD CORRESPONDINGLY INCREASE OR DECREASE, AS THE CASE MAY BE, THE ADB LENDING RATE BY FIVE BASIS POINTS ONLY. MOREOVER, IN THE EVENT THAT THE DIFFERENTIAL BETWEEN THE TWO LENDING RATES INCREASED OR DECREASED DURING THE THIRD AND/OR THE LAST QUARTERS OF THIS YEAR BY MORE THAN FIVE BASIS POINTS BEYOND THAT EXISTING IN THE FIRST CALENDAR

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QUARTER, THE POSITION MAY BE REVIEWED AND SUITABLE PROPOSALS SUBMITTED TO THE BOARD. WHEN IBRD FIXED ITS LENDING RATE AT 7.50 PERCENT PER ANNUM WITH EFFECT FROM APRIL 1, PRESIDENT ACCORDINGLY FIXED ADB'S LENDING RATE AT 7.70 PERCENT PER ANNUM WITH EFFECT FROM APRIL 1.

2. IBRD HAS FIXED ITS LENDING RATE AT 7.90 PERCENT WITH

EFFECT FROM JULY 1. THE ADB LENDING RATE WHICH WAS 20 BASIS POINTS MORE THAN THE IBRD LENDING RATE PRIOR TO JULY 1 HAS NOW BECOME 20 BASIS POINTS LESS THAN THE IBRD RATE.

3. ADB MANAGEMENT HAS ISSUED DOC. R63-78 WHICH EXAMINES THE IMPLICATIONS OF THIS SITUATION FOR THE BANK'S LENDING RATE. DOCUMENT WAS POUCHED JULY 7 AND WILL BE CONSIDERED BY BOARD OF DIRECTORS ON JULY 27.

4. DOCUMENT NOTES THAT CHANGE IN IBRD RATE ARISES PRIMARILY FROM METHOD IT USES TO AUTOMATICALLY DETERMINE ITS LENDING RATE, WHICH GIVES CONSIDERABLE WEIGHT TO BORROWINGS IN IMMEDIATELY PRECEDING QUARTER. LAST FEBRUARY, ADB BOARD OF DIRECTORS DECIDED IT WAS NOT ADVISABLE FOR THIS BANK TO ADOPT SUCH A FORMULA. ACCORDING TO ADB GUIDELINES: (A) THE LENDING RATE SHOULD BE BASED ON CRITERIA RELEVANT TO ITS OWN FINANCIAL STRUCTURE AND FINANCIAL STRENGTH AND RELATED TO ITS OWN BORROWING COSTS AND ADMINISTRATIVE EXPENSES; (B) AUTOMATIC ADJUSTMENT THROUGH A RIGID FORMULA MAY NOT BE ADVANTAGEOUS; AND (C) ADB SHOULD NOT EVEN APPEAR TO DIRECTLY TIE ITS LENDING RATE TO THAT OF IBRD.

5. AT TIME OF REVIEW IN EARLY 1978 OF ADB'S FINANCIAL POLICIES, COST OF NEW BORROWINGS IN 1978 WAS ASSUMED TO LIMITED OFFICIAL USE

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BE 7.90 PERCENT PER ANNUM. ACTUAL COST OF BORROWINGS SO FAR THIS YEAR IS SIGNIFICANTLY LOWER THAN THAT FOUND PRUDENT TO ASSUME IN BEGINNING OF YEAR. ACCORDING TO PRESENT INDICATIONS (EVEN ASSUMING A POSSIBLE 25-YEAR BORROWING IN U.S. MARKET AT AROUND 9.5 PERCENT) MANAGEMENT BELIEVES OVERALL COST OF 1978 BORROWINGS WOULD NOT WARRANT AN INCREASE NOW IN ADB LENDING RATE. THEY ALSO BELIEVE THAT THE DECISIVE FINANCIAL INDICATORS IN LONG-TERM FINANCIAL PROJECTIONS (I.E., INTEREST COVERAGE RATIO AND RESERVE: LOAN RATIO) AND FINANCIAL POSITION OF BANK NOW DO NOT WARRANT ANY INCREASE IN LENDING RATE AT THIS TIME. ADB MANAGEMENT, THEREFORE CONCLUDES THAT THERE DOES NOT APPEAR TO BE ANY CASE NOW FOR CHANGING BANK'S LENDING RATE DESPITE RECENT INCREASE IN IBRD LENDING RATE. MOREOVER, ADB MANAGEMENT BELIEVES THAT, SINCE FINANCIAL POSITION AND DECISIVE FINANCIAL INDICATORS ARE NOT LIKELY TO BE AFFECTED BY DEVELOPMENTS DURING REMAINING HALF OF THIS YEAR, AND IN INTEREST OF QUOTE SMOOTH FLOW OF WORK UNQUOTE, IT APPEARS SOUND POLICY NOT TO ENVISAGE A CHANGE IN THE ADB LENDING RATE IN THE LAST QUARTER OF THE YEAR. MANAGEMENT THEREFORE PROPOSES THAT ADB LENDING RATE, INCLUSIVE OF ONE PERCENT COMMISSION,

ON LOANS APPROVED BETWEEN JULY 1 AND DECEMBER 31, 1978
FROM BANK'S ORDINARY CAPITAL RESOURCES SHALL CONTINUE
TO BE 7.70 PERCENT PER ANNUM.

6. USADB COMMENT: MANAGEMENT'S PROPOSAL TO MAINTAIN
THE CURRENT RATE CLEARLY IS THE ADB'S STRONGEST EFFORT
TO DATE TO DISTANCE ITSELF FROM THE IBRD'S RATE DETER-
MINATION CRITERIA AND TO BASE THE ADB'S RATE ON ITS OWN
INTERNAL FINANCIAL INDICATORS AND BORROWING COSTS.

- ITS BORROWINGS SO FAR THIS YEAR IN JAPAN AND SWITZER-
LAND HAVE BEEN AT VERY FAVORABLE RATES OF INTEREST (6.3

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NSAE-00 XMB-02 OPIC-03 LAB-04 SIL-01 /117 W
-----070614 100721Z /21

P 100652Z JUL 78
FM AMEMBASSY MANILA
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FOR NAC AGENCIES

PASS TREASURY FOR SHERK

PERCENT AND 4.25 PERCENT RESPECTIVELY), AND APPARENTLY
THERE IS NO LONGER ANY NEED FOR THE ADB TO PAY A PREMIUM
OVER THE IBRD IN THOSE FINANCIAL MARKETS. THE ADB
EXPECTS TO BORROW AN ADDITIONAL SFR 100,000,000 (APPROXI-
MATELY DOLS 53.4 MILLION AS OF 6/30/78) FOR 10 YEARS AT
A RATE OF 4-3/8 PERCENT PER ANNUM.

- THE USADB HAS NOTED PRESS REPORTS THAT THE IBRD HAS
ANNOUNCED THAT IT WILL CONCENTRATE ITS BORROWING IN
MARKETS OUTSIDE THE UNITED STATES FOR THE REMAINDER OF
THE YEAR. ASSUMING THE ACCURACY OF THE ABOVE, THE IBRD

LENDING RATE FORMULA WHICH IS HEAVILY WEIGHTED TOWARD
BORROWING COSTS IN THE TWO MOST RECENT QUARTERS SHOULD
AGAIN BE REDUCED IN THE FOURTH QUARTER OF THIS YEAR.
NAC GUIDANCE IS REQUESTED. EDMOND

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Message Attributes

Automatic Decaptioning: X
Capture Date: 01 jan 1994
Channel Indicators: n/a
Current Classification: UNCLASSIFIED
Concepts: LOANS, INTEREST RATES
Control Number: n/a
Copy: SINGLE
Draft Date: 10 jul 1978
Decaption Date: 01 jan 1960
Decaption Note:
Disposition Action: RELEASED
Disposition Approved on Date:
Disposition Case Number: n/a
Disposition Comment: 25 YEAR REVIEW
Disposition Date: 20 Mar 2014
Disposition Event:
Disposition History: n/a
Disposition Reason:
Disposition Remarks:
Document Number: 1978MANILA11485
Document Source: CORE
Document Unique ID: 00
Drafter: n/a
Enclosure: n/a
Executive Order: N/A
Errors: N/A
Expiration:
Film Number: D780281-1034
Format: TEL
From: MANILA USADB
Handling Restrictions: n/a
Image Path:
ISecure: 1
Legacy Key: link1978/newtext/t19780779/aaaacoyq.tel
Line Count: 173
Litigation Code IDs:
Litigation Codes:
Litigation History:
Locator: TEXT ON-LINE, ON MICROFILM
Message ID: 3c796078-c288-dd11-92da-001cc4696bcc
Office: ACTION TRSE
Original Classification: LIMITED OFFICIAL USE
Original Handling Restrictions: n/a
Original Previous Classification: n/a
Original Previous Handling Restrictions: n/a
Page Count: 4
Previous Channel Indicators: n/a
Previous Classification: LIMITED OFFICIAL USE
Previous Handling Restrictions: n/a
Reference: n/a
Retention: 0
Review Action: RELEASED, APPROVED
Review Content Flags:
Review Date: 04 may 2005
Review Event:
Review Exemptions: n/a
Review Media Identifier:
Review Release Date: n/a
Review Release Event: n/a
Review Transfer Date:
Review Withdrawn Fields: n/a
SAS ID: 2067353
Secure: OPEN
Status: NATIVE
Subject: REVIEW OF ADB LENDING RATE
TAGS: EAID, EFIN, ADB
To: STATE
Type: TE
vdkgvwkey: odbc://SAS/SAS.dbo.SAS_Docs/3c796078-c288-dd11-92da-001cc4696bcc
Review Markings:
Sheryl P. Walter
Declassified/Released
US Department of State
EO Systematic Review
20 Mar 2014
Markings: Sheryl P. Walter Declassified/Released US Department of State EO Systematic Review 20 Mar 2014